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266 file

10 April 1985

MEMORANDUM FOR THE RECORD

SUBJECT: West European Efforts to reduce trade deficits with the USSR

In response to a request from SOVA/EPD/FT [redacted], I forwarded the attached country papers -- covering West Germany, France, the United Kingdom, and Italy -- on 10 April 1985. DAS Vargo at Commerce asked SOVA to pull together a typescript that will look at prospects for Soviet imports from the developed countries and LDCs. Commerce apparently is trying to determine how much the United States can expect to increase exports to the Soviet Union in the face of competition from other countries. Our contribution to the typescript addresses what the major West European countries are doing to reduce their bilateral trade deficits with the USSR; it probably will be used as an appendix to the SOVA paper. 25X1

State Dept. review completed

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DC/EURA/WE

Attachments:
(As stated)

EUR M85-10068
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ADDI
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EURA Production Staff (2)
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West Germany

Bonn is not overly concerned about its trade deficit with the USSR and is not applying pressure on Moscow to end the imbalance. The bilateral trade balance shifted from a $240 million (fob/fob) surplus in 1983 to a $750 million deficit last year. Bonn continues to run a comfortable global trade surplus. 25X1

West Germany has not initiated any projects or set up any special credit facilities to boost exports to the USSR. Officially-backed export credits are available to the USSR and to other countries with good credit ratings. During a January 1985 meeting of the Soviet-German Joint Economic Commission in Bonn, West German participation in development projects to be included under the next Soviet five year plan (1985-1990) was discussed. The West Germans expect, as in past Soviet plans, to capture a large portion of the Soviet contracts. 25X1

Bonn may focus more on its trade imbalance with the USSR if the deficit becomes structural. Gas deliveries over the next decade will rise about 25% in volume, while West German exports associated with pipeline development are winding down. If its global trade surplus is reduced by a future decline in the US dollar, Bonn might begin to actively pressure Moscow to buy more West German products. 25X1

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France

Of the major West European countries, France has complained the most to the Soviets over its continuing trade deficit. Although France recorded trade surpluses with the USSR between 1973 and 1979, after the second oil shock the trade balance has been consistently in the red. The deficit peaked at $1.5 billion in 1981 and exceeded $600 million last year. Energy imports, which account for over 85% of French imports from the Soviet Union, increased by 10 percent in 1984 as deliveries from the Siberian pipeline project began to flow in, and gas imports are scheduled to increase again this year. On the export side, almost one-half of all French sales to the USSR are agricultural goods, while semi-manufactured goods and finished manufactured goods each account for about another 25 percent. 25X1

France and the USSR signed an agreement in early 1984 that committed the Soviets to move toward balancing trade by increasing their purchases from the French. Nonetheless, exports to the USSR in 1984 fell in volume terms. From the French perspective, the most disturbing trend in Franco Soviet trade is the Soviet failure to place orders for capital equipment. Since the Socialists came to power, orders have fallen from over $1.5 billion (FF8 billion) in 1981 to less than $120 million (FF1 billion) last year -- the lowest level since the late 1960s. 25X1

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Until recently, the French had done little more than verbally protest over the deficit problem. In the last several weeks, however, they have adopted a more active approach. Renault has cancelled a deal to build an automobile plant, stating publicly that the Soviets had placed most of their equipment orders with West German firms, rather than with Renault or other French companies. In addition, press stories before the early April meeting of the Franco-Soviet Large Comission meeting suggested that France would reduce purchases of natural gas if Moscow did not increase imports of French capital equipment. Finally, on the eve of the Commission meeting Le Monde published the names of 47 Soviet "diplomats" ousted from France in 1983 for industrial espionage. It also published a Soviet document that outlines how Moscow uses trade and technical exchanges for industrial espionage. Le Monde implicitly admitted that the French internal security service had leaked the information. [redacted] 25X1
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Nevertheless, the French will continue to actively court the Soviets as customers. Paris is currently trying to get the Soviets to accept credits in European Currency Units in order to offer lower interest rates and compete more effectively with the FRG. After the early April meeting, Foreign Trade Minister Cresson said she wanted to wipe out the bilateral deficit this year and expected contracts for French gas equipment worth over $400 million to be signed soon. [redacted] 25X1

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United Kingdom

Britain does not view its trade deficit with the Soviet Union as a serious problem. Although the deficit with the Soviets grew from $32 million in 1970 to a peak of $875 million in 1979, since then it has come down appreciably and by 1984 was only $160 million. 25X1

Despite London's relative lack of concern, the British are attempting to increase exports to the Soviet Union. London and Moscow recently have resumed trade talks curtailed following the Soviet invasion of Afghanistan. British companies hope to land major contracts to sell petrochemical, chemical, and biotechnology processes to the Soviets this year. In his December visit to London, General Secretary Gorbachev said he saw "good opportunities" for British companies in the areas of machinery, agriculture, food processing, and chemicals in the Soviet Union. 25X1

In the past, the UK has been willing to offer attractive credit terms to promote exports to the Soviet Union and we believe London will continue using exports credits to increase trade in the future. 25X1

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Italy

The trade imbalance with the Soviet Union has been increasing steadily since 1974. The deficit climbed over the billion-dollar plateau in 1980, and last year's deficit reached a record $2.5 billion. Italy has recorded a trade surplus with the USSR in only 3 of the past 20 years. The Italians are eager to correct their trade deficit with the USSR but have yet to take strong measures to deal with the problem. 25X1

Italian officials are frustrated by the lack of progress in reducing the trade imbalance and have considered cutting back on fuel purchases, according to the US Embassy in Rome. More recently, however, they appear to have shelved this option because Italy faces a possible protracted renegotiation of its gas contract with Algeria that may make Soviet supplies more necessary. Italian-Soviet commerce is based primarily on the exchange of Soviet energy for Italian industrial products. The lion's share of Italian imports, about 90 percent, are oil and gas, while about 80 percent of Italian exports consist of steel and machinery. Soviet oil, purchased mainly on the spot market, accounts for about 14 percent of petroleum imports and has been attractively priced. This year, however, Soviet prices are out of line, and Italian oil companies will reduce their imports of Soviet petroleum, according to US Embassy sources. 25X1

Rome has two natural gas contracts with the Soviets which provided Italy with about 24 percent of its total gas supplies last year. The first, signed in 1969 and amended in 1974,

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requires Italy to buy 6.7 BCM of gas annually under take-or-pay provisions and expires in the year 2000. The second, a contract for Siberian gas signed in May 1984, runs until 2008. SNAM, the Italian state gas company, is currently negotiating with Soviet officials in hopes of bringing the pricing provisions of the 1969 agreeement down to the level of the second accord, about $3.60 per million BTUs. [redacted] 25X1

The Siberian gas accord, pushed strongly by the Italian business community, was accompanied by a commercial agreement committing the Soviets to cut the $1.7 billion 1983 deficit in half by 1986 and to spend the income from the new gas contract on Italian goods and services. The Soviet commitment was made, however, with the stipulation that Italian goods be competitive both in price and financing. A multitude of cooperation and collaboration agreements followed in almost every industrial field but despite initial business euphoria over the prospects of stepped up sales, actual contract signings have not lived up to expectations. [redacted] 25X1

Italian officials constantly remind the Soviets about their concern over the deficit and the lukewarm nature of Moscow's trade commitment. Italian goods, however, are priced in lire and dollars, placing their financing at a disadvantage compared to their major West European competitors because lira-and dollar-demoninated loans carry high interest rates. Under pressure from the Italians the Soviets grudgingly agreed last month to accept European Currency Units (ECUs) for contracts with Italian firms. Because the ECU reference interest rate is still well

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above what Italy's competitors offer and the Soviets will accept, Italian companies may also have to cover some of the financing cost by increasing prices or reducing profit margins. 25X1

Despite numerous setbacks, Italian officials are optimistic that they are on the verge of expanding exports to the Soviet Union and cutting back the trade deficit. Numerous small contracts were signed in 1984, and two fairly large contracts have been concluded this year. One contract, a joint venture between an Austrian and an Italian firm, is for producing steel cord for radial tires. The contract is valued at $220 million for the Italian firm Danieli, which absorbed one point to lower the financing cost to 7.5 percent over five years. The Italian company Cogolo will construct three shoe factories for a total of $60 million. 25X1

Italian officials also report that negotiations are underway for about $5 billion in additional contracts. Several contracts are reportedly ready to be signed, including the construction of a one million metric ton-a-year turn-key steel plant at Volgograd valued at about $1 billion, a $200-million oil-drilling-pipe plant, a $70-million coal slurry pipeline project in Novisibirsk, and about $750 million in contracts with Fiat. 25X1

Italian companies also hope to concude contracts for turn-key textile, chemical, and agroindustrial projects. IRI, the Italian state holding company, expects to participate in Soviet plans to modernize its steel industry, and the Soviets have expressed interest in Italian technology for flexible manufacturing equipment, automated assembly lines and gas

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injection equipment to increase output from ageing oil fields. [redacted]

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